

Exhibit No. 2Date 4-9-07

House Bill 63 -- PROPOSAL TO ACTUARIALLY FUND THE ~~TEACHERS' RETIREMENT SYSTEM~~ HB 63

**Sponsor: Representative John Musgrove**

**By Request of the Teachers' Retirement Board**

Testimony in support presented by:

David L. Senn, Executive Director

444-3376

April 9, 2007

**Constitutional & Funding Requirements**

The Montana Constitution, Article VIII, Section 15, requires all public retirement systems to be actuarially funded. The Teacher Retirement Board's Funding Policy states that whenever the amortization period of the unfunded liabilities for two consecutive valuations are projected to exceed 30 years through the use of long term cash flow projections, or the funded ratio is less than 85%, and the Board cannot reasonably anticipate that the amortization period would decline or the funded ratio improve without an increase in funding sources, it is the obligation of the Board to recommend to the legislature that funding be increased and/or liabilities be reduced. This proposal includes amendments to both increase funding and reduce liabilities.

The July 1, 2006, Actuarial Valuation for the Teachers' Retirement System (TRS) shows that largely due to market declines of 2001 and 2002 the current contribution rates will not amortize the unfunded liability over any period of time, and that the funded ratio is only 76%. A contribution rate increase of 3.38%, or a combination of rate increases and cash infusions are required to make the system actuarially sound. The Legislature must also eliminate loopholes that put stress on the actuarial soundness of the System, otherwise continued contribution rate increases, and/or cash infusions will be required to maintain the actuarial soundness of the TRS. The TRS unfunded liability is currently \$863.1 million, of which approximately \$395.5 million cannot be amortized with current contributions.

In their 2005 and 2006 audits of the TRS, the Legislative Auditor recommended, "legislation be enacted to provide funding to ensure the Teachers' Retirement System is funded on an actuarially sound basis, as required by the Montana Constitution". House Bill 63, as amended, includes adequate funding required to fund the TRS on an actuarially sound basis.

• **New funding sources - (Sections 1, 2, 6 & 11)**

The proposal to actuarially fund the System includes a one-time infusion of \$50 million, plus two graded contribution rate increases: 2.0% effective July 1, 2007, and an additional 0.38% increase on July 1, 2009. These rates will be paid by the State General Fund and will not be passed on to school districts. HB 63 will **NOT** increase property taxes.

- **Eliminate the statutory minimum rate of interest that may be credited by the Board – (Section 5)**

Given the market declines of the past few years, this rate should be set by the Board using a prudent standard related to market return. It is not reasonable to credit 4.0% interest if the system is making less than 4.0%.

- **Increase the MUS ORP supplemental contribution rate – (Section 7)**

The University System's Optional Retirement Plan (ORP) supplemental contribution rate must be increased 0.68%, from 4.04% to 4.72% if their unfunded liabilities that existed when the ORP was created are to be amortized by July 1, 2033, as required by current law. Without this increase, the TRS would not be actuarially sound.

- **Eliminate the statutory requirement that the Board increase GABA to 3.0% as funds become available – (Section 9)**

It is unrealistic to expect the Board to increase benefits when the legislature has not provided the additional revenue needed to fund the benefit enhancement. Under current law, any increase made by the TRS Board would create additional unfunded liabilities, with no additional funding to pay for them other than future excess investment earnings. This changes will not reduce the 1.5% GABA paid to all current and future retirees.

- **Close loopholes that create additional unfunded liabilities – (Sections 3, 4 & 10)**

**Clarify the State's policy on Teachers' Retirement** – Clarify that it is the state's policy to provide equitable benefits based on the member's normal service and salary and to limit spiking and double dipping opportunities.

*Two proposed changes will affect a few retirees who return to work in a position covered under the Teachers' Retirement System. Under TRS statutes, a retiree may return to work in a **part-time** position and earn up to the greater of **1/3** of the median average final compensation of those retired in the preceding fiscal year, or an amount not to exceed **1/3** of their average final compensation, plus CPI increases.*

**Revising the definitions of full-time and part-time service** – Full-time service is currently defined as "service that is full-time and that extends over a normal academic year of at least 9 months". Under this proposal, full-time service would be defined as 180 days or 140 hours per month over at least 9 months; part-time service would be defined as service that is less than full-time. Clearly defining part-time service will close the loophole currently used by retirees to work essentially full-time after retirement in a TRS eligible position. In fact, we recently discovered that a few of these "working retirees" have been reported as being employed full-time on their employer's Annual Data Collection (ADC) report submitted to Office of Public Instruction (OPI), and "part-time" for TRS purposes.

In September 2006, we followed-up with several districts that had reported working retirees on their 2005 ADC report as being employed full-time, while reporting these same folks to TRS as working part-time. While there were many reasons, most often we were told that their OPI report was in error; we also received responses similar to the following:

The ADC report was filed with OPI to indicate the position was based on a full-time service for the 240 days of the stated contract, not full-time of a normal 260-day contract used for TRS reporting purposes.

A preliminary review of the 2006 ADC data shows over 40 retirees in full-time positions, and many are the same retirees reported as working full-time in 2005. The ADC reports and the responses we received clearly demonstrated the need to define what constitutes part-time service under the Teachers' Retirement System.

Clarifying the maximum amount of compensation a retired member may earn under certain circumstances - During any school year 500 – 600 retirees are reported to TRS as having returned to work in a part-time position. Our review of the ADC reports and Department of Labor and Industry (DLI) wage records indicates that there may be as many as 1,200 retirees returning to work each year. Most only work a few days, but a few work the entire year in positions paying the maximum they can earn under TRS statutes, **PLUS** additional fringe benefits excluded from the definition of earned compensation under §19-20-101(6), MCA. This practice results in benefits being paid before a member actually terminates and retires; thus, increasing the total benefits paid by the System, which in turn increases the unfunded liabilities of the TRS.

HB 63 would include all remuneration paid to the retired member, excluding some fringe benefits, such as, employer paid health insurance premiums; employer provided housing; reimbursement of employment-related travel expenses and de minimis fringe benefits as defined by the IRS.

### **Why is closing the loopholes important?**

Today, only around 20% of the TRS members retire when they are first eligible. If 100% members were able to start drawing benefits when first eligible and continue working in a TRS covered position, 80% would be under funded, and contributions would need to increase at least another 3.0%, or around \$20 million per year.

Essentially the loopholes provide the opportunity for a few individuals to continue working almost full-time, receive a full salaries and full retirement benefits. If these loopholes are not addressed by this legislation, or in other bills, the funded ratio of the TRS will continue to decline, and additional contributions will be required.

Today only a handful of retirees are able to negotiate contracts to take advantage of the loopholes. (Some entities have stated fewer than 10.) However, in a recent comparison of the TRS retiree database with the OPI Annual Data Collection report and wage reports from the Department of Labor, we found over 50 retirees with wages reported to DLI that were greater than the maximum the retiree was eligible to earn under TRS statutes. The highest wage in this group exceeded \$70,000, and this was

for someone who was eligible to earn \$27,664. The difference is fringe benefits not reported as compensation to TRS, such as a \$2,000 per month housing allowance and a \$1,000 car allowance.

### **Summary**

None of the changes proposed in HB 63 can solve the Teachers' Retirement System funding dilemma by themselves. Taken together, however, they move the TRS forward in meeting our constitutional obligation to actuarially fund the system. The impacts are shared between the State, employers, and retirees.

The TRS is currently \$863.1 million under funded, and if HB 63 is approved as is, the unfunded liabilities will amortize over 33.2 years. There is no room to amend this bill to provide any additional benefit enhancements, such as expanded return to work provisions. This is a difficult challenge, but one we must resolve.

The Teachers' Retirement Board asks that you concur with HB 63 as is and resist any attempts to amend HB 63 which would remove the loophole closures or enhance return to work provisions.

*Employment Contract Examples*

serves the DISTRICT subject to approval of the Board; shall from time to time suggest regulations, rules and procedures for the Board's consideration, and in general, perform all duties incident to the position and such other duties as may be prescribed by the Board from time to time. In the event that the accreditation standards as applied to the District change for any reason, including but not limited to, modification to the accreditation standards, growth of the District, during the term of this contract, the parties shall renegotiate any applicable material provisions of the agreement. Should the parties be unable to reach an agreement regarding any such material provisions, such a change in accreditation requirements shall constitute good cause for purposes of terminating this agreement.

C. Outside Activities: ADMINISTRATOR shall devote his time, attention and energy to the business of the school district as set forth in Paragraph 2.B. above. So long as any other activity does not impact his ability to perform the essential functions of his position within the District, he may serve as consultant to other districts or educational agencies, lecture, engage in writing activities and speaking engagements, and engage in other activities which are of a short-term duration. If this outside activity requires that ADMINISTRATOR be absent from his position with the District, he will be required to use vacation or personal leave. In no case will DISTRICT be responsible for any expenses attributable to the performance of such outside activities.

3. **PROFESSIONAL GROWTH OF ADMINISTRATOR**: DISTRICT encourages the continuing professional growth of ADMINISTRATOR through his participation in:

- A. The operations, programs, and other activities conducted or sponsored by local, state, and national school administrators and school Board associations;
- B. Seminars and courses offered by public or private educational institutions; and,
- C. Informational meetings with other persons whose particular skills or backgrounds would serve to improve the capacity of ADMINISTRATOR to perform his professional responsibilities for DISTRICT.

DISTRICT agrees to allocate Twenty Four Hundred Dollars (\$2,400.00) annually for ADMINISTRATOR'S discretionary professional leave/travel.

4. **COMPENSATION**: DISTRICT shall pay ADMINISTRATOR at an annual salary of Twenty Four Thousand (\$24,000) for the 2005-2006 school year. This annual rate shall be paid to ADMINISTRATOR in monthly installments of one/twelfth of the annual salary rate on the \_\_\_\_ day of each month for his services rendered during the current month. This amount shall increase in subsequent years of this contract by an amount equal to the consumer price index for urban wage earners compiled by the Bureau of Labor Statistics of the United States Department of Labor or its successor agency in the preceeding year.

5. **LEAVE OF ABSENCE**: ADMINISTRATOR shall accrue sick and vacation leave as

prescribed in Title 2, Chapter 18, Part 6. Additionally, \_\_\_ days of non-accumulative personal leave shall be granted each year.

6. **OTHER BENEFITS:** DISTRICT will offer the following additional benefits to ADMINISTRATOR under the terms of this Contract:

- A. Housing Allowance - DISTRICT will pay ADMINISTRATOR Two Thousand Dollars (\$2000.00) per month as a housing allowance.
- B. Automobile Allowance - DISTRICT will pay ADMINISTRATOR One Thousand Dollars (\$1000.00) per month as an automobile allowance.
- C. 457 Contribution - DISTRICT will contribute Three Thousand Dollars (\$3000.00) annually to ADMINISTRATOR'S 457 account.
- D. Health, Disability and Other Insurance - DISTRICT will pay an annual amount of Five Thousand Five Hundred Dollars (\$5500.00) toward ADMINISTRATOR'S health insurance under DISTRICT'S current health plan.
- E. Signing Bonus - DISTRICT will pay ADMINISTRATOR a Twenty Five Hundred (\$2500.00) signing bonus in year one of this Contract.
- F. Moving Expenses - DISTRICT will reimburse ADMINISTRATOR expenses reasonably incurred for the moving of furnishings from the ADMINISTRATOR'S present residence to his new residence in the Bozeman area. The reimbursement shall be based on actual receipts, shall be subject to approval of the Board of Trustees as to reasonableness, and shall in no event exceed a total of Five Thousand Dollars (\$5,000.00). Any money left over from the Five Thousand Dollars (\$5,000.00) moving expense allotment may be directed toward health insurance premiums for year one of the contract.

In order to further comply with the provisions of Section 19-20-804, MCA, and other applicable provisions, the fringe benefits provided to ADMINISTRATOR as set forth in Paragraph 6 and as proposed by ADMINISTRATOR are not to be regarded as earned compensation for purposes of TRS and are specifically excluded from the definition of "earned compensation" as that term is defined in Section 19-20-101, MCA. The parties agree and acknowledge, however, that this agreement is only binding as to the parties to this agreement and not on third-parties, including but not limited to the TRS and the IRS. The parties further agree and acknowledge that the District has no control over the decisions made at TRS and IRS and should TRS at any time make a determination that ADMINISTRATOR'S eligibility under TRS is affected by this Agreement or the IRS make a determination to the detriment of ADMINISTRATOR, the District shall have no obligations to provide compensation to ADMINISTRATOR other than that specifically provided for in this agreement. Administrator further agrees to defend, indemnify, and hold

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**PART I:**

**1. Term.** The Board, by and on behalf of the District, employs the Superintendent, and the Superintendent accepts part-time employment as District Superintendent for the District for a term of one (1) year from August 1, 2006 to June 30, 2007. Teachers Retirement System

**2. Renewal.** Upon the offer and acceptance of the second successive Contract, the second and subsequent Contracts will be deemed to be renewed at the end of each term for a further term of one (1) year thereafter, unless the Board, by resolution passed by a majority vote of its membership prior to February 1 in the last year of such Contract, resolves to terminate the services of the Superintendent at the expiration of the existing Contract.

**3. Duties.** The Superintendent is the chief executive officer of the District and shall perform the duties of District Superintendent for the District as prescribed in the job description and as may be assigned by the Board. The Superintendent shall comply with legal Board directives, section 20-4-402, MCA, and other applicable state and federal law, District policies as they exist or may hereafter be adopted or amended, which are incorporated in and made a part of this Contract as though fully set forth herein. The Superintendent agrees to devote his or her time and energy to the performance of these duties in a faithful manner.

**4. Professional Activities.** The Superintendent may attend and participate in appropriate professional meetings at the local, state and national levels with the reasonable expenses for such attendance to be borne by the District, including membership fees and dues of the Superintendent in such organization. Appropriate and reasonable shall include those meetings and expenses incorporated into the budget or otherwise pre-approved by the Board.

**5. Professional Certification and Records.** This Agreement is conditioned on the Superintendent's providing the necessary certification and experience records and other records required for the personnel files or for payroll purposes. Failure to provide necessary certification shall render this Agreement void. Any misrepresentation may be grounds for dismissal.

**6. Reassignment.** The Superintendent shall not be reassigned from the position of Superintendent to another position during the term of the Contract without the mutual written consent of the parties. Reassignment shall not be construed, however, as including the assignment of additional administrative duties as part of a reduction in the number of administrators in the district.

X **7. Compensation.** The Board agrees to pay the Superintendent for his or her services an annual salary of Twenty eight thousand Dollars (\$ 28,000.00), paid in equal monthly installments unless otherwise agreed to by the parties.

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BOARD OF TRUSTEES CHAIR

\_\_\_\_\_  
DISTRICT SUPERINTENDENT

\_\_\_\_\_  
DISTRICT CLERK

5-15-06

DATE

5/18/06

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5-17-06

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Teachers Retirement System

## PART II:

### Professional Dues

The Board shall pay the Association dues of the Superintendent for the School Administrators of Montana and the SAM Region in which the School District is located, as well as other appropriate affiliations, and civic and social memberships as approved by the Board.

### Transportation

The Board shall provide the Superintendent with an automobile for business use. The school District shall incur and pay the cost of: insurance, all maintenance for the assigned automobile; and gasoline for business mileage.

The Superintendent shall maintain a log of business and personal use of the assigned automobile. Personal use mileage shall be reflected as income on the W-2 form issued to the superintendent each year.

The Board shall reimburse the Superintendent for use of his or her automobile in conducting business on behalf of the District in accordance with section 2-18-503, MCA.

### Health, Disability, and Other Insurance

The District shall pay the premium for coverage for group health and hospitalization, dental and vision insurance for the Superintendent in accordance with the District's plan of insurance and shall provide the Superintendent with all other benefits on the same basis as other classified employees of the District.

### Fringe Benefit or Non-Earned Compensation

X The Board agrees to pay the Superintendent for his or her services an annual salary of Twelve thousand Dollars (\$ 12,000.00), paid in installments unless otherwise agreed to by the parties.

X The District shall pay the following: \$700.00/month housing allowance and \$3,600.00 annual insurance payment (Thrivent Long Term Care Policy # N0707021 and Thrivent Life Insurance